98TH CONGRESS
2d Session

HOUSE OF REPRESENTATIVES

REPORT
98-1050

ONE-YEAR EXTENSION OF EXCLUSION WITH RESPECT TO GROUP LEGAL SERVICES PLANS

SEPTEMBER 24, 1984.—Committed to the Committee of the Whole House on the State of the Union and ordered to be printed

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Mr. ROSTENKOWSKI, from the Committee on Ways and Means, submitted the following

REPORT

together with

ADDITIONAL VIEWS

[To accompany H.R. 5361]

[Including cost estimate of the Congressional Budget Office]

The Committee on Ways and Means, to whom was referred the bill (H.R. 5361), to extend for 1 year the exclusion from gross income with respect to group legal services plans, and for other purposes, having considered the same, report favorably thereon with amendments and recommend that the bill as amended do pass.

The amendments are as follows:

Strike out all after the enacting clause and insert in lieu thereof the following:

SECTION 1. AMENDMENTS RELATING TO QUALIFIED GROUP LEGAL SERVICES PLANS.

(a) 1-YEAR EXTENSION OF EXCLUSION FROM GROSS INCOME.—Subection (e) of section 120 of the Internal Revenue Code of 1954 (relating to amounts received under qualified group legal services plans) is amended by striking out "December 31, 1984" and inserting in lieu thereof "December 31, 1985".

(b) REPORTING AND RECORDKEEPING REQUIREMENTS.—

(1) IN GENERAL.—Subpart A of part III of subchapter A of chapter 61 of such Code is amended by inserting after section 6039C the following new section:

"SEC. 6039D. RETURNS AND RECORDS WITH RESPECT TO CERTAIN FRINGE BENEFIT PLANS.

"(a) IN GENERAL.—Every employer maintaining a specified fringe benefit plan during any year beginning after December 31, 1984, for any portion of which the applicable exclusion applies, shall file a return (at such time and in such manner as the Secretary shall by regulations prescribe) with respect to such plan showing for such year—

"(1) the number of employees of the employer,

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"(2) the number of employees of the employer eligible to participate under the plan,

"(3) the number of employees participating under the plan,

"(4) the total cost of the plan during the year, and

"(5) the name, address, and taxpayer identification number of the employer an the type of business in which the employer is engaged.

"(b) RECORDKEEPING REQUIREMENT.—Each employer maintaining a specified fringe benefit plan during any year shall keep such records as may be necessary for purposes of determning whether the requirements of the applicable exclusion are met.

"(c) ADDITIONAL INFORMATION WHEN REQUIRED BY THE SECRETARY.—Any employer—

"(1) who maintains a specified fringe benefit plan during any year for which a return is required under subsection (a), and

"(2) who is required by the Secretary to file an additional return for such year,

shall file such additional return. Such additional return shall be filed at such time and in such manner as the Secretary shall prescribe and shall contain such information as the Secretary shall prescribe.

"(d) DEFINITIONS.—For purposes of this section—

"(1) SPECIFIED FRINGE BENEFIT PLAN.—The term 'specified fring benefit plan' means—

"(A) any qualified group legal services plan (as defined in section 120), and

"(B) any cafeteria plan (as defined in section 125).

"(2) APPLICABLE EXCLUSION.—The term 'applicable exclusion' means—

"(A) section 120, in the case of a qualified group legal services plan, and

"(B) section 125, in the case of a cafeteria plan."

(2) PENALTY.—Subsection (f) of section 6652 of such Code (relating to failure to file certain information returns, registration statements, etc.) is amended by striking out "125(h) (relating to information with respect to cafeteria plans)" and inserting in lieu thereof "6039D (relating to returns and records with respect to certain fringe benefit plans)".

(3) CONFORMING AMENDMENTS.—

(A) Section 120 of such Code is amended by adding at the end thereof the following new subsection:

"(f) CROSS REFERENCE.—

"For reporting and recordkeeping requirements, see section 6039D."

(B) Section 125 of such Code (relating to cafeteria plans) is amended by striking out subsection (h) and inserting in lieu thereof the following:

"(h) CROSS REFERENCE.—

"For reporting and recordkeeping requirements, see section 6039D."

(4) CLERICAL AMENDMENT.—The table of sections for subpart A of part III of subchapter A of chapter 61 of such Code is amended by inserting after the item relating to section 6039C the following new item:

"Sec. 6039D. Returns and records with respect to certain fringe benefit plans."

(c) EXCLUSION FROM RAILROAD RETIREMENT TAXES FOR AMOUNTS WHICH MAY BE EXCLUDED UNDER SECTION 120.—Subsection (e) of section 3231 of such Code (defining compensation for purposes of the railroad retirement taxes) is amended by adding at the end thereof the following new paragraph:

"(6) The term 'compensation' shall not include any contribution, payment, or service provided by an employer which may be excluded from the gross income of an employee, his spouse, or his dependents, under the provisions of section 120 (relating to amounts received under qualified group legal services plans)."

(d) EFFECTIVE DATES.—

(1) SUBSECTION (a).—The amendment made by subsection (a) shall apply to taxable years ending after December 31, 1984.

(2) SUBSECTION (b).—The amendments made by subsection (b) shall take effect on January 1, 1985.

(3) SUBSECTION (c).—The amendment made by subsection (c) shall apply to remuneration paid after December 31, 1984.

Amend the title so as to read:

A bill to amend the Internal Revenue Code of 1954 to extend for 1 year the exclusion from gross income with respect to group legal services plans, and for other purposes.

I. Summary

Under present law, amounts contributed by an employer to a qualified group legal services plan for employees (or their spouses or dependents) are excluded from an employee's gross income for income and employment tax purposes. Present law also provides that an organization created exclusively to form part of a qualified group legal services plan may be exempt from income tax. The exclusion for prepaid legal services and the tax exemption for group legal services organizations are scheduled to expire for taxable years ending after December 31, 1984.

The bill extends the exclusion for qualified group legal services plans and the tax exemption for group legal services organizations for one year. In addition, the bill requires an employer with a group legal services plan to provide an annual information return on the plan to the Internal Revenue Service.

II. EXPLANATION OF THE BILL

Present Law

General rule

Under present law, amounts contributed by an employer to a qualified group legal services plan for employees (or their spouses or dependents) are excluded from an employee's gross income for income and employment tax purposes. The exclusion also applies to any services received by an employee or any amounts paid to an employee under such a plan as reimbursement for legal services for the employee (or the employee's spouse or dependents).

In order to be a qualified plan under which employees are entitled to tax-free benefits, a group legal services plan must fulfill several requirements with regard to its provisions, the employer, and the covered employees.

Legal services

A qualified group legal services plan must be a separate written plan of an employer for the exclusive benefit of employees or their spouses or dependents. The plan must supply the employees, their spouses, and dependents with specified benefits consisting of personal (i.e., nonbusiness) legal services through prepayment of, or provision in advance for, all or part of the legal fees of an employee or an employee's spouse or dependent.

Present law also provides that amounts contributed by employers under a qualified group legal services plan may be paid only (1) to insurance companies or to organizations or persons that provide personal legal services or indemnification against the cost of personal legal services, in exchange for a prepayment or a payment of a premium; (2) to organizations exempt from taxation as organizations described in section 501(c)(20) (see below for description); (3) to tax-exempt organizations described in section 501(c) that are permitted to receive employer contributions for one or more qualified group legal services plans, provided the organizations pay or credit the employer contributions to another organization that is described in section 501(c)(20); (4) as prepayments to providers of legal

services under the plan; or (5) to a combination of the four permissible types of payment arrangements.

Nondiscrimination

In order to be a qualified plan, a group legal services plan must also meet requirements with respect to nondiscrimination in contributions or benefits and in eligibility for enrollment.

Present law requires that the contributions paid by an employer and the benefits provided under a plan may not discriminate in favor of employees who are officers, shareholders, self-employed individuals, or highly compensated. The plan must benefit employees who qualify under a classification that the employer sets up and that the Internal Revenue Service determines does not discriminate in favor of employees who are officers, shareholders, self-employed individuals, or highly compensated. However, in determining whether a classification is discriminatory, the employer may exclude from the calculation those employees who are members of a collective bargaining unit if there is evidence that group legal services plan benefits were the subject of good faith bargaining between employee representatives and the employer.

A limit is placed on the poroportion of the amounts contributed under the plan that can be applied for employees who own more than five percent of the stock or of the capital or profits interest in the employer corporation or unincorporated trade or business. The aggregate of the contributions for those employees and their spouses and dependents must not be more than 25 percent of the total contributions.

Other rules

Under present law, in order to be treated as a qualified group legal services plan, the plan must notify the Internal Revenue Service that it is applying for recognition of qualified status. If the plan fails to notify the IRS by the time prescribed in Treasury regulations, then the plan is not regarded as a qualified plan for any period before it, in fact, gave notice.

A self-employed individual who qualifies as an employee within the definition of Code section 401(c)(1) is also an employee for purposes of these group legal services provisions. This means that, in general, the term self-employed individual means, and the term employee includes, individuals who have earned income for a taxable year, as well as individuals who would have earned income except that their trades or businesses did not have net profits for a taxable year. An individual who owns the entire interest in an unincorporated trade or business is treated as his or her own employer. A partnership is considered the employer of each partner who is also an employee of the partnership.

Group legal services organizations

Present law also provides that an organization or trust created or organized in the United States whose exclusive function is to form part of a qualified group legal services plan is exempt from income tax (sec. 501(c)(20)). Such a trust is subject to the rules generally governing organizations exempt from taxation under section 501(a), including the rules relating to the taxation of any unrelated

business income. An exempt organization or trust that receives employer contributions for a group legal services plan is not prevented from qualifying for exemption under section 501(c)(20) merely because it provides legal services or indemnification for legal services unassociated with a qualified group legal services plan.

Termination

The present-law exclusion for prepaid legal services and the tax exemption for group legal services organizations are scheduled to expire for taxable years ending after December 31, 1984.

Reasons for Change

The committee recognizes that although the group legal services exclusion was enacted for only a temporary period in order to provide the Congress with an opportunity to evaluate the exclusion, the absence of any information reporting requirements has made it difficult to obtain information concerning the operation of these plans. The committee believes that it is appropriate to extend the exclusion for one additional year and to adopt an annual information return requirement, so that the Treasury Department and Internal Revenue Service will have data relating to the use and effectiveness of the exclusion. The committee anticipates that a comprehensive examination of the effect of the exclusion of this and other statutory fringe benefits on the income, wage, and benefit bases will be necessary next year.

In addition, the committee recognizes that the Tax Reform Act of 1976 (sec. 2134(d)) required the Treasury Department and the Department of Labor to submit a report on the use and effectiveness of group legal services plans. Therefore, the committee has decided not to direct the Treasury Department to submit a new study, but rather the committee emphasizes its expectation that the Treasury Department will expeditiously comply with the earlier statutory requirement of a study.

Explanation of Provisions

Extension of exclusion

The bill provides that the group legal services exclusion and the tax exemption for group legal services organizations is to expire for taxable years ending after December 31, 1985. Thus, the provisions are extended for one additional year.

Reporting requirements

The bill requires any employer maintaining a group legal services plan during any year to file an information return with respect to the plan at the time and in the manner required by Treasury regulations. The return is to show (1) the number of employees of the employer, (2) the number of employees eligible to participate in the plan, (3) the number of employees participating in the plan, (4) the total cost of the plan during the year, and (5) the name, address, and taxpayer identification number of the employer and the type of business in which the employer is engaged.

Under the bill, each employer maintaining a group legal services plan during any year is to keep any records that may be necessary in order to determine whether the plan meets the requirements relating to group legal services plans.

The bill provides that the Secretary may require employers to file an additional return for any year in addition to the information return. The additional return is to be filed at such time and in such manner as the Secretary may prescribe and is to contain such information as the Secretary may require.

The penalty for failure to file the returns required by the bill is the same penalty that generally applies to failures to file certain information returns (sec. 6652). The return filing requirement is not required to be satisfied for any portion of any year during which the provision excluding group legal services benefits is in effect.

Exclusion from railroad retirement taxes

The bill provides that the group legal services exclusion also applies to the wage base for purposes of the railroad retirement taxes.

Effective Dates

The provisions of the bill generally are effective for taxable years ending after December 31, 1984. The reporting and recordkeeping requirements of the bill take effect on January 1, 1985. The railroad retirement provision is effective for remuneration paid after December 31, 1984.

III. BUDGET EFFECTS OF THE BILL AND VOTE OF THE COMMITTEE

A. Budget Effects

In compliance with clause 7 of Rule XIII of the Rules of the House of Representatives, the following statement is made about the effect on the budget of the provisions of H.R. 5361 as reported by the committee.

The following table provides estimates of the income tax and social security tax effects of the bill as amended for fiscal years 1985–1989.

FISCAL YEARS

[Millions of dollars]

	1985	1986	1987	1988	1989
Income tax	−39	−16			
Social Security	−15	−5			
Total	−54	−21			

The Treasury Department agrees with this statement.

B. Vote of the Committee

In compliance with clause 3(1)(2)(B) of Rule XI of the Rules of the House of Representatives, the following statement is made about the vote of the committee on the motion to report H.R. 5361 as amended. The bill, as amended by the committee, was ordered favorably reported by voice vote.

IV. OTHER MATTERS TO BE DISCUSSED UNDER HOUSE RULES

In compliance with clauses 2(1)(3) and 2(1)(4) of rule XI of the Rules of the House of Representatives, the following statements are made with respect to the committee action on H.R. 5361, as amended.

Oversight Findings

With respect to Subdivision (A) of clause 2(1)(3) (relating to oversight findings), the commitee advises that it was as a result of the committee's review of expiring tax provisions (in this case, regarding the tax-exempt status of qualified group legal plans for employees and plan benefits for employers, which expires at the end of 1984) that the committee concluded that it was appropriate to extend the exclusion for one year (through 1985). This will allow the committee additional time to review the provision.

The Subcommittee on Select Revenue Measures held a hearing on the bill as introduced on April 12, 1984. (As introduced, the bill would have provided for a 5-year extension of the exclusion.) The full committee considered the bill on September 19, 1984, and ordered it favorably reported with an amendment (for a one-year extension).

Tax Expenditures

With respect to subdivision (B) of clause 2(1)(3), after consultation with the Director of the Congressional Budget Office, the committee states that the chagnes made by the bill as reported involve an extension of an existing tax expenditure of $39 million in fiscal year 1985 and $16 million in fiscal year 1986.

New Budget Authority

With respect to subdivision (B) of clause 2(1)(3), after consultation with the Director of the Congressional Budget Office, the committee states that the changes made by the bill as reported involve no new budget authority.

Congressional Budget Office Estimates

With respect to subdivision (C) of clause 2(1)(3), the committee advises that the Director of the Congressional Budget Office has examined the committee's budget estimates (as indicated in Part III of this report) and agrees with the budget estimates. The Director submitted the following statement.

U.S. CONGRESS,
CONGRESSIONAL BUDGET OFFICE,
Washington, DC, September 20, 1984.

Hon. DAN ROSTENKOWSKI,
Chairman, Committee on Ways and Means, U.S. House of Representatives, Washington, DC.

DEAR MR. CHAIRMAN: The Congressional Budget Office has reviewed H.R. 5361, as ordered reported by the Committee. The bill would extend for one year (until December 31, 1985) the exclusion for employer-provided services.

The CBO has reviewed and concurs with estimates of the bill's revenue effect prepared by the staff of the Joint Committee on Taxation. The bill would reduce fiscal year revenues by $54 million in 1985 and $21 million in 1986, and increase fiscal year tax expenditures by $39 million in 1985 and $16 million in 1986. The bill would not affect budget outlays.

With best wishes.

Sincerely,

RUDOLPH G. PENNER.

Oversight by Committee on Government Operations

With respect to subdivision (D) of clause 2(1)(3), the committee advises that no oversight findings or recommendations have been submitted to the committee by the Committee on Government Operations regarding the subject matter of the bill.

Inflationary Impact

In compliance with clause 2(1)(4), the committee states that the enactment of the bill, H.R. 5361 as amended, is not expected to have any inflationary impact on prices and costs in the operation of the national economy.

V. Changes in Existing Law Made by the Bill, As Reported

In compliance with clause 3 of rule XIII of the Rules of the House of Representatives, changes in existing law made by the bill, as reported, are shown as follows (existing law proposed to be omitted is enclosed in black brackets, new matter is printed in italics, existing law in which no change is proposed is shown in roman):

INTERNAL REVENUE CODE OF 1954

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Subtitle A—Income Taxes

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CHAPTER 1—NORMAL TAXES AND SURTAXES

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Subchapter B—Computation of Taxable Income

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PART III—ITEMS SPECIFICALLY EXCLUDED FROM GROSS INCOME

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SEC. 120. AMOUNTS RECEIVED UNDER QUALIFIED GROUP LEGAL SERVICES PLANS.

(a) EXCLUSION BY EMPLOYEE FOR CONTRIBUTIONS AND LEGAL SERVICES PROVIDED BY EMPLOYEE.—Gross income of an employee, his spouse, or his dependents, does not include—

(1) amounts contributed by an employer on behalf of an employee, his spouse, or his dependents under a qualified group legal services plan (as defined in subsection (b)); or

(2) the value of legal services provided, or amounts paid for legal services, under a qualified group legal services plan (as defined in subsection (b)) to, or with respect to, an employee, his spouse, or his dependents.

(b) QUALIFIED GROUP LEGAL SERVICES PLAN.—For purposes of this section, a qualified group legal services plan is a separate written plan of an employer for the exclusive benefit of his employees or their spouses or dependents to provide such employee, spouses, or dependents with specified benefits consisting of personal legal services through prepayment of, or provision in advance for, legal fees in whole or in part by the employer, if the plan meets the requirements of subsection (c).

(c) REQUIREMENTS—

(1) DISCRIMINATION.—The contributions or benefits provided under the plan shall not discriminate in favor of employees who are officers, shareholders, self-employed individuals, or highly compensated.

(2) ELIGIBILITY.—The plan shall benefit employees who qualify under a classification set up by the employer and found by the Secretary not to be discriminatory in favor of employees who are described in paragraph (1). For purposes of this paragraph, there shall be excluded from consideration employees not included in the plan who are included in a unit of employees covered by an agreement which the Secretary of Labor finds to be a collective bargaining agreement between employee representatives and one or more employers, if there is evidence that group legal services plan benefits were the subject of good faith bargaining between such employee representatives and such employer or employers.

(3) CONTRIBUTION LIMITATION.—Not more than 25 percent of the amounts contributed under the plan during the year may be provided for the class of individuals who are shareholders or owners (or their spouses or dependents), each of whom (on any day of the year) owns more than 5 percent of the stock or of the capital or profits interest in the employer.

(4) NOTIFICATION.—The plan shall give notice to the Secretary, in such manner as the Secretary may by regulations pre-

scribe, that it is applying for recognition of the status of a qualified group legal services plan.

(5) CONTRIBUTIONS.—Amounts contributed under the plan shall be paid only (A) to insurance companies, or to organizations or persons that provide personal legal services, or indemnification against the cost of personal legal services, in exchange for a prepayment or payment of a premium, (B) to organizations or trusts described in section 501(c)(20), (C) to organizations described in section 501(c) which are permitted by that section to receive payments from an employer for support of one or more qualified group legal services plan or plans, except that such organizations shall pay or credit the contribution to an organization or trust described in section 501(c)(20), (D) as prepayments to providers of legal services under the plan, or (E) a combination of the above.

(d) OTHER DEFINITIONS AND SPECIAL RULES.—For purposes of this section—

(1) SELF-EMPLOYED INDIVIDUAL EMPLOYEE.—The term "self-employed individual" means, and the term "employee" includes, for any year, an individual who is an employee within the meaning of section 401(c)(1) (relating to self-employed individuals).

(2) EMPLOYER.—An individual who owns the entire interest in an unincorporated trade or business shall be treated as his own employer. A partnership shall be treated as the employer of each partner who is an employee within the meaning of paragraph (1).

(3) ALLOCATIONS.—Allocations of amounts contributed under the plan shall be made in accordance with regulations prescribed by the Secretary and shall take into account the expected relative utilization of benefits to be provided from such contributions of plan assets and the manner in which any premium or other charge was developed.

(4) DEPENDENT.—The term "dependent" has the meaning given to it by section 152.

(5) EXCLUSIVE BENEFIT.—In the case of a plan to which contributions are made by more than one employer, in determining whether the plan is for the exclusive benefit of an employer's employees or their spouses or dependents, the employees of any employer who maintains the plan shall be considered to be the employees of each employer who maintains the plan.

(6) ATTRIBUTION RULE.—For purposes of this section—

(A) ownership of stock in a corporation shall be determined in accordance with the rules provided under subsections (d) and (e) of section 1563 (without regard to section 1563(e)(3)(C)), and

(B) the interest of an employee in a trade or business which is not incorporated shall be determined in accordance with regulations prescribed by the Secretary, which shall be based on principles similar to the principles which apply in the case of subparagraph (A).

(7) TIME OF NOTICE TO SECRETARY.—A plan shall not be a qualified group legal services plan for any period prior to the time notification was provided to the Secretary in accordance

with subsection (c)(4), if such notice is given after the time prescribed by the Secretary by regulations for giving such notice.

(e) TERMINATION.—This section and section 501(c)(20) shall not apply to taxable years ending after December 31, [1984.] *1985.*

(f) CROSS REFERENCE.—

For reporting and recordkeeping requirements, see section 6039D.

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SEC. 125. CAFETERIA PLANS.

(a) IN GENERAL—* * *

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[(h) REPORTING REQUIREMENTS—

[(1) IN GENERAL—Each employer maintaining a cafeteria plan during any year which begins after December 31, 1984, and to which this section applies shall file a return (at such time and in such manner as the Secretary shall by regulations prescribe) with respect to such plan showing for such year—

[(A) the number of employees of the employer,

[(B) the number of employees participating under the plan,

[(C) the total cost of the plan during the year, and

[(D) the name, address, and taxpayer identification number of the employer and the type of business in which the employer is engaged.

[(2) RECORDKEEPING REQUIREMENT—Each employer maintaining a cafeteria plan during any year shall keep such records as may be necessary for purposes of determining whether the requirements of this section are met.

[(3) ADDITIONAL INFORMATION WHEN REQUIRED BY THE SECRETARY—Any employer—

[(A) who maintains a cafeteria plan during any year for which a return is required under paragraph (1), and

[(B) who is required by the Secretary to file an additional return for such year,

shall file such additional return. Such additional return shall be filed at such time and in such manner as the Secretary shall prescribe and shall contain such information as the Secretary shall prescribe.]

(h) CROSS REFERENCE.—

For Reporting and recordkeeping requirements, see section 6039D.

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Subtitle C—Employment Taxes and Collection of Income Tax at Source

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CHAPTER 22—RAILROAD RETIREMENT TAX ACT

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Subchapter D—General Provisions

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SEC. 3231. DEFINITIONS.

(a) EMPLOYER—* * *

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(e) COMPENSATION.—For purposes of this chapter—

(1) The term "compensation" means any form of money remuneration paid to an individual for services rendered as an employee to one or more employers. Such term does not include (i) the amount of any payment (including any amount paid by an employer for insurance or annuities, or into a fund, to provide for any such payment) made to, or on behalf of, an employee or any of his dependents under a plan or system established by an employer which makes provision for his employees generally (or for his employees generally and their dependents) or for a class or classes of his employees (or for a class or classes of his employees and their dependents), on account of sickness or accident disability or medical or hospitalization expenses in connection with sickness or accident disability, (ii) tips (except as is provided under paragraph (3)), or (iii) an amount paid specifically—either as an advance, as reimbursement or allowance—for traveling or other bona fide and necessary expenses incurred or reasonably expected to be incurred in the business of the employer provided any such payment is identified by the employer either by a separate payment or by specifically indicating the separate amounts where both wages and expense reimbursement or allowance are combined in a single payment. Such term does not include remuneration for service which is performed by a nonresident alien individual for the period he is temporarily present in the United States as a nonimmigrant under subparagraph (F) or (J) of section 101(a)(15) of the Immigration and Nationality Act, as amended, and which is performed to carry out the purpose specified in subparagraph (F) or (J), as the case may be. For the purpose of determining the amount of taxes under sections 3201 and 3221, compensation earned in the service of a local lodge or division of a railway-labor-organization employer shall be disregarded with respect to any calendar month if the amount thereof is less than $25. Compensation for service as a delegate to a national or international convention of a railway labor organization defined as an "employer" in subsection (a) of this section shall be disregarded for purposes of determining the amount of taxes due pursuant to this chapter if the individual rendering such service has not previously rendered service, other than as such a delegate, which may be included in his "years of service" for purposes of the Railroad Retirement Act.

(2) APPLICATION OF CONTRIBUTION BASES.—

(A) COMPENSATION IN EXCESS OF APPLICABLE BASE EXCLUDED—

(i) IN GENERAL.—The term "compensation" does not include that part of remuneration paid during any calendar year to an individual by an employer after remuneration equal to the applicable base has been paid during such calendar year to such individual by such employer for services rendered as an employee to such employer.

(ii) REMUNERATION NOT TREATED AS COMPENSATION EXCLUDED.—There shall not be taken into account under clause (i) remuneration which (without regard to clause (i)) is not treated as compensation under this subsection.

(B) APPLICABLE BASE.—

(i) TIER 1 TAXES.—Except as provided in clause (ii), the term "applicable base" means for any calendar year the contribution and benefit base determined under section 230 of the Social Security Act for such calendar year.

(ii) TIER 2 TAXES, ETC.—For purposes of—

(I) the taxes imposed by sections 3201(b), 3211(a)(2), and 3221(b), and

(II) computing average monthly compensation under section 3(j) of the Railroad Retirement Act of 1974 (except with respect to annuity amounts determined under subsection (a) or (f)(3) of section 3 of such Act),

clause (2) of the first sentence, and the second sentence, of subsection (c) of section 230 of the Social Security Act shall be disregarded.

(C) SUCCESSOR EMPLOYERS.—For purposes of this paragraph, the second sentence section 3121(a)(1) (relating to successor employers) shall apply, except that—

(i) the term "services" shall be substituted for "employment" each place it appears,

(ii) the term "compensation" shall be substituted for "remuneration (other than remuneration referred to in the succeeding paragraphs of this subsection)" each place it appears, and

(iii) the terms "employer", "services", and "compensation" shall have the meanings given such terms by this section.

(3) Solely for purposes of the taxes imposed by section 3201 and other provisions of this chapter insofar as they relate to such taxes, the term "compensation" also includes cash tips received by an employee in any calendar month in the course of his employment by an employer unless the amount of such cash tips is less than $20.

(4)(A) For purposes of applying sections 3201(a), 3211(a)(1), and 3221(a), in the case of payments made to an employee or any of his dependents on account of sickness or accident disability, clause (i) of the second sentence of paragraph (1) shall exclude from the term "compensation" only—

(i) payments which are received udner a workmen's compensation law, and

(ii) benefits received under the Railroad Retirement Act of 1974.

(B) Notwithstanding any other provision of law, for purposes of the sections specified in subparagraph (A), the term "compensation" shall include benefits paid under section 2(a) of the Railroad Unemployment Insurance Act for days of sickness, except to the extent that such sickness (as determined in accordance with standards prescribed by the Railroad Retirement Board) is the result of on-the-job injury.

(C) Under regulations prescribed by the Secretary, subparagraphs (A) and (B) shall not apply to payments made after the expiration of a 6-month period comparable to the 6-month period described in section 3121(a)(4).

(D) Except as otherwise provided in regulations prescribed by the Secretary, any third party which makes a payment included in compensation solely by reason of subparagraph (A) or (B) shall be treated for purposes of this chapter as the employer with respect to such compensation.

(5) The term "compensation" shall not include any benefit provided to or on behalf of an employee if at the time such benefit is provided it is reasonable to believe that the employee will be able to exclude such benefit from income under section 117 or 132.

(6) The term "compensation" shall not include any contribution, payment, or service provided by an employer which may be excluded from the gross income of an employee, his spouse, or his dependents, under the provisions of section 120 (relating to amounts received under qualified group legal services plans).

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Subtitle F—Procedure and Administration

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CHAPTER 61—INFORMATION AND RETURNS

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Subchapter A—Returns and Records

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PART III—INFORMATION RETURNS

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Subpart A—Information Concerning Persons Subject to Special Provisions

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Sec. 6039D. Returns and records with respect to certain fringe benefits plans.

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SEC. 6039D. RETURNS AND RECORDS WITH RESPECT TO CERTAIN FRINGE BENEFIT PLANS.

(a) IN GENERAL.—Every employer maintaining a specified fringe benefit plan during any year beginning after December 31, 1984, for any portion of which the applicable exclusion applies, shall file a return (at such time and in such manner as the Secretary shall by regulations prescribe) with respect to such plan showing for such year—

(1) the number of employees of the employer,

(2) the number of employees of the employer eligible to participate under the plan,

(3) the number of employees participating under the plan,

(4) the total cost of the plan during the year, and

(5) the name, address, and taxpayer identification number of the employer and the type of business in which the employer is engaged.

(b) RECORDKEEPING REQUIREMENT.—Each employer maintaining a specified fringe benefit plan during any year shall keep such records as may be necessary for purposes of determining whether the requirements of the applicable exclusion are met.

(c) ADDITIONAL INFORMATION WHEN REQUIRED BY THE SECRETARY.—Any employer—

(1) who maintains a specified fringe benefit plan during any year for which a return is required under subsection (a), and

(2) who is required by the Secretary to file an additional return for such year,

shall file such additional return. Such additional return shall be filed at such time and in such manner as the Secretary shall prescribe and shall contain such information as the Secretary shall prescribe.

(d) DEFINITIONS.—For purposes of this section—

(1) SPECIFIED FRINGE BENEFIT PLAN.—The term "specified fringe benefit plan" means—

(A) any qualified group legal services plan (as defined in section 120), and

(B) any cafeteria plan (as defined in section 125).

(2) APPLICABLE EXCLUSION.—The term "applicable exclusion" means—

(A) section 120, in the case of a qualified group legal services plan, and

(B) section 125, in the case of a cafeteria plan.

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CHAPTER 68—ADDITIONS TO THE TAX, ADDITIONAL AMOUNTS, AND ASSESSABLE PENALTIES

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Subchapter A—Additions to the Tax and Additional Amounts

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SEC. 6652. FAILURE TO FILE CERTAIN INFORMATION RETURNS, REGISTRATION STATEMENTS, ETC.

(a) RETURNS RELATING TO INFORMATION AT SOURCE, PAYMENTS OF DIVIDENDS, ETC., AND CERTAIN TRANSFERS OF STOCK.—

(1) IN GENERAL.— * * *

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(f) INFORMATION REQUIRED IN CONNECTION WITH CERTAIN PLANS OF DEFERRED COMPENSATION, ETC.—In the case of failure to file a return or statement required under section 6058 (relating to information required in connection with certain plans of deferred compensation), 6047 (relating to information relating to certain trusts and annuity and bond purchase [sic] plans), or [125(h) (relating to information with respect to cafeteria plans)] *6039D (relating to returns and records with respect to certain fringe benefit plans)* on the date and in the manner prescribed therefor (determined with regard to any extension of time for filing), unless it is shown that such failure is due to reasonable cause, there shall be paid (on notice and demand by the Secretary and in the same manner as tax) by the person failing so to file, $25 for each day during which such failure continues, but the total amount imposed under this subsection on any person for failure to file any return shall not exceed $15,000.

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VI. ADDITIONAL VIEWS OF THE HONORABLE J.J. PICKLE

In the past decade, tax exempt employee benefits have grown at a phenomenal rate. It becomes a matter of great public importance if government allows a continued large growth in employee benefits which permits a business to deduct, as a business expense, certain salary costs, and in turn allows the employee to avoid payment of tax on the benefits. While a great deal of good comes from these employee benefits, there is also an erosion of the federal tax bases. Businesses and employees can't always have it both ways—without Uncle Sam being the loser. I think the Congress should make an earnest effort to find the proper balance in the tax treatment of employee benefits programs.

I support enactment of H.R. 5361 which provides an extension of the exemption, through 1985, from income and employment taxes for prepaid legal assistance programs. However, I expect a thorough review of this provision in 1985 and I do not believe that prepaid legal assistance benefits should also be exempt from employment taxes, as has been provided in this bill. These benefits should be subject to the employment taxes.

I make these statements not because I am opposed to fringe benefits or seek to eliminate the prepaid legal assistance program. Rather, there are strong arguments which lead me to the conclusion that prepaid legal assistance can be encouraged without also eroding a worker's social security coverage.

Those who oppose the imposition of employment taxes on prepaid legal assistance make three arguments; all without foundation. These arguments are:

(1) the social security and income tax bases should be identical;

(2) the imposition of FICA taxes on prepaid legal assistance will kill these programs;

(3) the imposition of FICA taxes will bear most heavily on those who can least afford to pay them.

There is no compelling reason to have identical wage bases for social security and income tax purposes. In fact, the two wage bases have always been dissimilar and the 1983 Social Security Amendments specifically stated that Congress does not want to require completely identical wage bases.

The income tax and the social security tax have very different purposes. The income tax is designed solely to raise revenue; the social security program is a social insurance program which replaces a worker's income if he should die, retire or become disabled. FICA taxes are imposed solely to finance those insurance benefits.

Given the different purpose of the social security program, why should workers be forced to choose between prepaid legal assistance and future social security benefits?

Taxing the benefits for FICA purposes does not discriminate against low-income workers, who can least afford to pay the tax. The group which should most concern Congress is the dependents or survivors of workers. This is the group for whom social security is designed to provide lost income in the form of social security benefits and who receive permanently reduced benefits as a result of the FICA tax exclusion which the worker chose at an earlier point.

If a worker excludes even a small portion of his wages, his benefit (and that of his dependents or survivors) can be drastically affected. For example, a worker, aged 60 with average earnings ($16,019) in 1984 who has $65 in prepaid legal services excluded from his social security wage and benefit base and a similar percent of his future earnings also excluded, saves $81 in taxes before January 1, 1989 when he retires. If the worker is single, the total amount of social security benefits which he has lost as a result of the exclusion is $816. The total amount of lost benefits is $1,404 if he is married.

The worker who is aged 21 in 1984 who has the same percent of his average earnings excluded through 1992 as a result of prepaid legal services benefits as shown above who dies leaving a wife and 2 children has saved $379 in FICA taxes but has lost $14,652 in social security benefits for his survivors.

While it is true that not all workers would be affected in this manner, such an experience is neither extreme, nor uncommon. It is because of just this kind of tragedy that survivors benefits are part of our social security insurance program.

Taxing these fringe benefits for FICA will not "kill" these programs. In the 1983 Social Security Amendments, Section 401(k) plans were taxed for FICA purposes and the program has continued to grow dramatically.

If Congress wants to encourage these benefits, there's more than enough incentive provided through the income tax exclusion.

Before concluding, let me put this bill in a broader perspective. On September 17 and 18, 1984, the Subcommittees on Social Security and Select Revenue Measures held hearings on the distribution and economics of statutory fringe benefits. We were presented with some rather alarming statistics. Between 1950 and 1984, employer-sponsored fringe benefits receiving tax-favored treatment increased from 2.6 to 10.4 percent of total compensation. The Social Security Trustees project that the ratio of benefits to total compensation will increase by 0.3 percent annually. According to SSA's Chief Actuary, by the year 2060, fringe benefits will represent some 34 percent of total compensation. It is clear that the projected growth of tax-favored fringe benefits will continue to erode both the income and payroll tax bases and raise the long-run costs of the social security program.

Prepaid legal assistance benefits are admittedly only a small portion of the problem. However, if we are unable to make the difficult decisions on these minor benefits, how will we respond to the more intense pressure exerted when all fringe benefits come under scrutiny next year? By refusing to impose FICA taxes on educational assistance benefits now, we are sending a signal to employers and employees everywhere to proceed full steam ahead with their plans to offer more tax-favored benefits to their employees in place of taxable compensation. We should be honest with ourselves and ask whether we can afford this growing drain on Federal revenues at this time?

In conclusion, I would note again that the tax exemptions in this legislation are extended only until December 31, 1985. During the coming year, I will continue to study the impact of this tax policy and I expect that the Subcommittee on Social Security will hold further hearings in this area.

As we proceed with this review, we must ask ourselves why should there be a social security tax exclusion to encourage the use of a fringe benefit, which has nothing to do with the purposes of the social security program, when there is sufficient incentive through the income tax exclusion, and when this exclusion forces workers to choose between that benefit and future social security benefits?

J.J. PICKLE.

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